82-1658

No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

PUBLIC SERVICE COMMISSION
OF THE DISTRICT OF COLUMBIA,
Petitioner,

v.

WASHINGTON GAS LIGHT COMPANY,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE DISTRICT OF COLUMBIA COURT OF APPEALS

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QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission exceeded its jurisdiction under the Natural Gas Act when it decided to approve the annual budgets of Gas Research Institute, a research, development and demonstration organization engaged in research into synthetic gas and other subjects beyond FERC's regulatory jurisdiction, and to authorize the cost of Gas Research Institute's activities to be added to the wholesale cost of natural gas, requiring State and local regulatory Commissions to pass that cost on to consumers.

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*Parties to the proceeding in the District of Columbia Court of Appeals, in addition to the Public Service Commission of the District of Columbia and Washington Gas Light Company, included the Office of People's Counsel of the District of Columbia. Gas Research Institute filed a brief as *amicus curiae*.

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OPINIONS BELOW

The opinion of the District of Columbia Court of Appeals which this petition seeks to have the court review is officially reported at 452 A.2d 375 (D.C. App. 1982). It is reproduced in the appendix, starting at 1a.

The orders of the Public Service Commission of the District of Columbia are reported at 39 PUR 4th 161 (D.C.P.S.C. 1980).[1] There is no official report. Pursuant

[1]The Commission first issued a proposed opinion and interim order. Excerpts are at 28a. Commissioner Long filed a partial concurring and dissenting opinion. The Commission then issued a final opinion and order. Excerpts are at 33a. Finally, the Commission issued an order denying applications for reconsideration. Excerpts are at 34a.

to authorization of the Clerk, ten copies of the orders of the Public Service Commission of the District of Columbia have been lodged with the Clerk's Office. Excerpts, containing all of those portions of the orders relevant to this petition are reproduced in the appendix, starting at 28a.

JURISDICTION

The Judgment of the District of Columbia Court of Appeals which this petition seeks to have the court review was entered on October 29, 1982. Petitioner filed a timely petition for rehearing in the District of Columbia Court of Appeals which that court denied without opinion on January 21, 1983. This petition is filed within 90 days of that date.

This court has jurisdiction to review the judgment of the District of Columbia Court of Appeals by writ of certiorari pursuant to 28 U.S.C. § 1257(3).

STATUTES

Natural Gas Act §§ 2, 4, 8 and 16.[2]

STATEMENT OF THE CASE

On June 29, 1979, Respondent Washington Gas Light Company ("Washington Gas") filed a rate increase application which led to proceedings before Petitioner Public Service Commission of the District of Columbia ("the Commission"). The proceedings were designated Formal Case No. 722. One of the issues which the Commission had to address in Formal Case No. 722 was whether it was

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[2]See Appendix, pp. 34a-41a.

required to permit Washington Gas to treat Washington Gas' costs for its allocable share of the budget of Gas Research Institute ("GRI") as an operating expense.

GRI is a research, development and demonstration organization whose members consist of wholesale and retail gas companies, including Washington Gas and its wholesale suppliers, Columbia Gas and Transco ("the pipelines"). GRI engages in research into a variety of gas related issues, much of it involving synthetic gas. The Federal Energy Regulatory Commission ("FERC") is authorized to regulate the wholesale price of natural gas under § 4 of the Natural Gas Act. Although FERC has no statutory authority to supervise or regulate research organizations, FERC decided to assume jurisdiction to approve GRIs' budgets and to authorize GRI to impose charges upon its members. Under this scheme, FERC authorized the member pipelines to include their GRI assessments in the wholesale price of natural gas to retailers, such as Washington Gas.

In Formal Case No. 722, the Commission decided to use the calendar year ending December 31, 1979 as its test year.[3] The Commission was then faced with deciding whether it was obliged by FERC preemption to permit Washington Gas to recover its GRI surcharges as operating expenses[4] without independently reviewing the reasonableness of those charges, as it must for all other such expenses.

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[3]Under District of Columbia law, the Commission engages in traditional test year ratemaking in which it examines the rate base, rate of return and expenses on the basis of a particular year's data and, if that year's data warrants it, authorizes a prospective change in public utility rates. See *Potomac Electric Power Co. v. Public Service Commission*, 402 A.2d 14 (D.C. App.), cert denied, 444 U.S. 926 (1979).

[4]During the test year, the GRI surcharge from the pipelines to Washington Gas was .047 center per therm.

Washington Gas contended that FERC's action in regulating GRI and authorizing GRI's expenses to be added as a surcharge to the wholesale cost of natural gas completely preempted state and local regulatory commissions from independently inquiring for retail ratemaking purposes into the reasonableness of Washington Gas' GRI payments. People's Counsel, a statutory party to Commission proceedings, contended that the Commission retained authority, despite FERC's approval of the surcharge, to determine whether Washington Gas' GRI expense was beneficial to District of Columbia ratepayers and, if the Commission determined that it was not, to refuse to permit Washington Gas to treat the surcharge as an operating expense for ratemaking purposes.

On October 3, 1980, the Commission issued its Proposed Opinion and Interim Order in Formal Case No. 722. (Excerpted at 28a) Having heard evidence on GRI's program, the Commission concluded that the benefits to the immediate consumer were "indirect at best" and will be substantially less to residential consumers than to industrial and commercial customers and to gas utility companies in general. (31a-32a) Although the Commission found that Washington Gas' stockholders stood to receive a substantially greater benefit from GRI than its customers, the Commission decided to allow Washington Gas' test year GRI charge as an operating expense because the amount was small and because there was some promise of benefit to consumers.[5]

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[5]The order noted that the Commission was aware that FERC's Opinion No. 64, which reviewed GRI, was under review on the preemption issue in *Public Utilities Commission of Colorado v. FERC*, 213 U.S. App. D.C. 1, 660 F.2d 821 (1981), cert denied, 456 U.S.____, 102 S.Ct. 2009 (1982), which was at that time still undecided.

Washington Gas filed exceptions to the Commission's proposed opinion. It noted that its GRI surcharge had been raised by an increase in the per therm rate, effective January 1, 1981, and sought to have the Commission reflect that change in its authorized retail rates. In its Final Opinion and Order, filed November 10, 1980, the Commission denied Washington Gas' exception. The Commission declined to approve the post-test year per term increase, because, "although approved by FERC, [it] has not been shown to be justified on a record before this Commission." (33a)

Washington Gas pressed the same issue by application for reconsideration, and, in an order entered December 24, 1980, the Commission ruled that, since *Public Utilities Commission of Colorado v. FERC, supra,* was still pending, the post-test year increase lacked the certainty necessary to require rate order adjustment. (34a)

On appeal to the District of Columbia Court of Appeals, Washington Gas raised the issue of Commission authority to deny automatic pass through of its GRI per therm surcharge, contending that the Commission was wholly preempted by FERC's assumption of jurisdiction over GRI. People's Counsel intervened in the appeal and argued that, despite FERC approval, the Commission retained authority to review GRI's potential benefit to ratepayers before approving expense treatment of the GRI surcharge. The Commission's position was that, until the District of Columbia Circuit finally decided the *Colorado* case, the GRI surcharge lacked the certainty to justify post-test year rate adjustment. Its contention was that, while it could not reexamine the appropriateness of a FERC – approved wholesale rate surcharge, it was not obliged to authorize the retail utility to pass through such

a surcharge if FERC's approval of it was *ultra vires*, the point in issue in the *Colorado* case.

While this case was pending before the District of Columbia Court of Appeals, the District of Columbia Circuit decided the Colorado case, affirming FERC's authority to regulate GRI. *Public Utilities Commission of Colorado v. FERC*, 213 U.S. App. D.C. 1, 660 F.2d 821 (1981). The Public Utilities Commission of Colorado bypassed suggesting rehearing *en banc* and sought review here.[6] On April 26, 1982, this court denied certiorari. 456 U.S.____, 102 S.Ct. 2009.

The Commission then was granted leave to file a supplemental memorandum in the District of Columbia Court of Appeals. The Commission requested the court to sustain its denial to Washington Gas of the post-test year adjustment on the alternative ground that, since FERC lacked authority to regulate GRI, the Commission was obliged to review Washington Gas' payments for GRI expenses before approving rate treatment. Noting that this court had denied *Colorado's* petition, the Commission contended that the District of Columbia Court of Appeals had authority to independently examine the issue of FERC jurisdiction and that it should do so, since such action would create the conflict which this court might see as necessary to grant review.[7] The Commission then argued

[6]The Commission and several state regulatory commissions filed briefs as *amici curiae* urging the court to accept the Colorado Case.

[7]Appellate review of FERC decisions can be sought in the District of Columbia Circuit or the circuit in which the natural gas company has its principal place of business. See *F.P.C. v. Texaco, Inc.*, 377 U.S. 33 (1954); 15 U.S.C. § 717r(b). Since GRI is not a natural gas company, the practical effect of the law is to limit review to the District of Columbia Circuit.

to the court of appeals that, since a large part of GRI's activities involved research into synthetic gas[8] or subjects far removed from natural gas and Congress had specifically denied FERC authority to regulate synthetic fuels,[9] FERC exceeded its authority when it undertook to regulate GRI and authorize rate treatment of its budget.

In an opinion filed October 29, 1982, the District of Columbia Court of Appeals held that the Commission had no authority to inquire into the reasonableness of the GRI surcharge. (20a) The court declined the Commission's request to hold that FERC had exceeded its jurisdiction, because "[r]eview of the rulings of FERC is vested by statute in the United States Court of Appeals, not this court."[10] (21a) The Commission's timely application for rehearing was denied January 21, 1983. (26a)

REASONS FOR GRANTING THE WRIT

It is important that the integrity of basic regulatory systems be maintained in the face of overreaching by FERC, that the careful balance which Congress ordained between federal and state regulation of interstate natural gas sales be defended.

The court below, however, squarely held that the Commission had no authority to disallow the GRI surcharge as

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[8]See *Public Utilities Commission of Colorado v. FERC, supra,* 660 F.2d at 825-826.

[9]See *Office of Consumer's Counsel v. FERC,* 210 U.S. App. D.C. 315, 655 F.2d 1132 (1980); *Public Service Commission of New York v. F.P.C.,* 177 U.S. App. D.C. 245, 543 F.2d 392 (1976); *Henry v. F.P.C.,* 168 U.S. App. D.C. 137, 513 F.2d 395 (1975).

[10]Since the court of appeals concluded that its reversal of the Commission on the GRI issue did not render the entire rate order unreasonable, it did not remand on that point for modification of the rate order. (24a-25a)

a reasonable operating expense and that the Commission was unauthorized to consider whether the GRI surcharge benefits District of Columbia ratepayers. As a consequence, the court has stripped those ratepayers of any meaningful protection — heretofore afforded by the D.C. Commission — from having to bear the cost of programs that may be of no benefit to them whatsoever.

GRI clearly is not a natural gas company within the meaning of the Natural Gas Act, for GRI, a research and development organization, is engaged neither in the transportation of natural gas in interstate commerce nor the sale of natural gas in interstate commerce for resale.[11] Thus no basis exists under the Natural Gas Act for FERC to regulate or approve GRI surcharges, much less to obligate state commissions[12] to pass those charges through to consumers without regard to any benefit therefrom for the local ratepayers.

The problem stems from the rule that, when FERC authorizes a charge to be placed on wholesale rates, regulators of retail sales of natural gas must permit the charges authorized by FERC to be passed on to the retail ratepayers as part of the cost of purchased gas. See, e.g., *Narragansett Electric Co. v. Burke,* 381 A.2d 1358 (R.I. 1977), cert. den., 435 U.S. 972 (1978). On the other hand, where FERC does not regulate a charge on wholesale rates, retail commissions, such as the D.C. Commission, may determine the reasonableness of the charge before adding it to the retail rates. Thus, any increase of FERC

[11]See FERC opinion No. 11 quoted in *Public Utilities Comm'n of Colorado v. FERC, supra,* 660 F.2d at 823.

[12]While the D.C. Commission is not a "state" regulatory commission and was created by an Act of Congress, it functions like a state commission in regulating retail natural gas sales.

regulatory jurisdiction decreases the regulatory jurisdiction of state retail commissions; FERC's usurpation of authority regarding GRI charges reduces the authority of state commissions. The decision below graphically illustrates that proposition and shows the harm that accordingly befalls retail ratepayers. Because of this harm, the direct result of overreaching by FERC, a writ of certiorari should issue to review the decision below.

It is important that courts and agencies maintain the integrity of basic regulatory systems mandated by Congress. That integrity is destroyed when loose and casual scrutiny by FERC of the potential benefit to ratepayers of GRI charges is substituted for the close scrutiny of the D.C. Commission.

It is also important that the integrity of basic regulatory systems created by Congress not fall prey to actions that run directly counter to the will of Congress.

Much of research and development work proposed to be undertaken by GRI involves something other than natural gas as such. See *Public Utilities Commission of Colorado v. FERC, supra,* 660 F.2d 821, 825 n.9. While it might be desirable for FERC to administer — and raise money for — a varied research program in the name of conservation of dwindling gas supplies, the fact remains that Congress has denied FERC such authority. The decision below conflicts with that decision of Congress.

Synthetic fuels provide the most obvious example of how overreaching by FERC given legal sanction by the decision below violates Congressional intent. Several of GRI's research areas concern synthetic fuels. Congress, however, has legislated on this subject, creating, *inter alia,* the Synthetic Fuels Corporation, 42 U.S.C.

§§ 8701 *et seq.*[13] Under the Act, the corporation may provide financial assistance of various types to research and development projects in an amount of up to $88 billion. See, e.g., 42 U.S.C. §§ 8772(c)(11), 8751. That munificent sum of money does not, however, come from gas ratepayers as such. Congress has determined that financial support for synthetic fuels development should come from sources other than ratepayers. Nothing in the Act refers to FERC or to ratepayers. FERC approval of GRI charges for synthetic fuels research conflicts with Congressional intentions.[15]

It is important that the decisional law in this area be both internally consistent and supportive of basic regulatory systems. The decision below, treats the *Colorado* decision as controlling. The latter decision is, however, directly inconsistent with *Henry v. F.P.C.*, 168 U.S. App. D.C. 137 513 F.2d 395 (1975) and *Office of Consumers' Counsel v. FERC*, 210 U.S. App. D.C. 315, 655 F.2d 1132 (1980).

In *Henry, supra*, three applications were filed before FERC pursuant to § 7(c) of the Natural Gas Act[15] for certificates of public convenience and necessity. The facilities involved included plant for the manufacture and transportation of synthetic gas and plant for the mixing of synthetic and natural gas. The court, affirming the FPC, held that the FPC had no jurisdiction over plant devoted to the

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[13]This legislation is part of the Energy Security Act of 1980, P.L. 96-294.

[14]The Energy Security Act of 1980 includes other titles concerning, *inter alia*, biomass energy and alcohol fuels, renewable energy initiatives, solar energy and energy conservation, and geothermal reservoirs. In none of these areas does it appear that Congress meant for FERC to saddle ratepayers with research costs.

[15]15 U.S.C.A. § 717f(c).

production or transportation of synthetic gas prior to its mixture with natural gas from wells.

In *Office of Consumers' Counsel, supra,* a consortium of natural gas companies sought a § 7(c) certificate for a coal gasification plant and a pipeline to transport the synthetic gas to a point where it would be commingled with natural gas and sold. FERC granted the application. On appeal the District of Columbia Circuit reversed, holding on the basis of *Henry* that FERC had no regulatory jurisdiction over any aspect of synthetic gas production or development prior to its commingling with natural gas. FERC had argued that its action merely authorized future sales of commingled gas. The court rejected the argument, finding that the proposal at issue was in fact a financing device rather than a gas supply project, that the hypothetical sale of commingled gas was remote in time, place and even probability, and that FERC would regulate the plant during the construction and preoperation period, a time during which, of course, there would be no synthetic gas from the plant to commingle with natural gas.

It is entirely clear, in light of *Henry* and *Office of Consumers' Counsel,* that FERC has no regulatory jurisdiction of synthetic gas plant. And yet the court below implements the *Colorado* decision, to the effect that FERC can nevertheless regulate and guarantee rate treatment of synthetic fuel research development and demonstration and for research into appliance, performance and technology, even though few of the GRI's research activities cited in the FERC opinions independently fall under FERC jurisdiction and even though none of them are any more closely related to a jurisdictional event — the transportation or sale for resale of natural gas — than was the plant at issue in *Office of Consumers' Counsel.*

The court below held that review of FERC actions was vested only in the United States Court of Appeals. If it is correct, it underscores the need for this court to consider the merits of this case; neither state supreme courts nor other circuits would have authority to decide the issue of FERC authority differently from the District of Columbia Circuit. Consequently only that court and this one can set matters right. Since the District of Columbia Circuit has not done so, only this court can. It is important that the writ of certiorari should issue for this purpose.

The decision of the court of appeals in *Public Utilities Commission of Colorado v. FERC, supra,* is in conflict with the same court's earlier opinion in *Office of Consumer's Counsel v. FERC,* 210 U.S. App. D.C. 315, 655 F.2d 1132 (1980). While there has been some expression that an intracircuit conflict is for the court of appeals itself to resolve through its en banc procedure,[16] the existence of such a conflict must be weighted with other factors in deciding whether to grant certiorari. For example, the combination of an intracircuit conflict with an important question does justify the issuance of a writ of certiorari. See *John Hancock Ins. Co. v. Bartels,* 308 U.S. 180, 181 (1939). See also *Scott v. United States,* 436 U.S. 128 (1978), in which the combination of conflicting views among the judges of the District of Columbia Circuit and the importance of the question led this court to grant certiorari where it had earlier denied the writ to the same issue presented on interlocutory review. In addition, where the area of the law is a specialized one and the problems have

[16]In *Davis v. United States,* 405 U.S. 933 (1972), the court denied certiorari when the solicitor general so argued. See *Davis v. United States,* 417 U.S. 333, 340 (1974). *Davis,* however, was a criminal case in which the litigant could and did present the issue again in a collateral proceeding. That is not the case here.

arisen and will continue to arise within one circuit,[17] it is most appropriate for this court to exercise its discretion to intervene and resolve the conflict. See *Maggio v. Zeitz*, 333 U.S. 56, 59-60 (1948). The latter category applies particularly to this case and the court from which it comes. See note 7, *supra*.

CONCLUSION

The court should issue a writ of certiorari to review the issue of FERC regulatory authority.

Respectfully submitted,

/s/ ____________________

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[17] In this instance, while the decision in *Public Utilities Commission of Colorado*, *supra*, was written for the District of Columbia Circuit, it was authorized by a visiting district judge.

APPENDICES

DISTRICT OF COLUMBIA COURT OF APPEALS

No. 81-229

WASHINGTON GAS LIGHT COMPANY, PETITIONER,

v.

PUBLIC SERVICE COMMISSION OF THE DISTRICT of COLUMBIA, RESPONDENT,

OFFICE OF PEOPLE'S COUNSEL OF THE DISTRICT of COLUMBIA, INTERVENOR.

No. 81-232

OFFICE OF PEOPLE'S COUNSEL OF THE DISTRICT of COLUMBIA, PETITIONER,

v.

PUBLIC SERVICE COMMISSION OF THE DISTRICT of COLUMBIA, RESPONDENT,

WASHINGTON GAS LIGHT COMPANY, INTERVENOR.

Petitions for Review of an Order of the Public Service Commission

(Argued September 24, 1981 Decided October 29, 1982)

Telemac N. Chryssikos, with whom *Lewis Carroll* and *Monte R. Edwards* were on the briefs, for petitioner in No. 81-229 and intervenor in No. 81-232.

Lloyd N. Moore, Jr., General Counsel, for respondent.

Elizabeth A. Noel, Deputy People's Counsel, with whom *Brian J. H. Lederer*, People's Counsel, was on the briefs, for intervenor in No. 81-229 and petitioner in No. 81-232.

James M. Broadstone, Christopher T. Boland, Peter C. Lesch, and *Steve Stojic* filed an amicus curiae brief on behalf of Gas Research Institute.

Before KELLY, HARRIS * and BELSON, *Associate Judges.*

BELSON, *Associate Judge*: Petitioner, Washington Gas Light Company (WGL or Company) sought a rate increase of $17.8 million. Cross petitioner, Office of People's Counsel (OPC) generally opposed it. On November 10, 1980 the Public Service Commission of the District of Columbia (PSC or Commission) awarded an increase of $11.9 million. Both WGL and OPC were dissatisfied and petitioned this court for redress. We conclude that the PSC made two erroneous rulings unfavorable to WGL, but that the errors were not consequential enough to warrant remand with instructions to grant relief. We also conclude that the Commission failed to explain its reasons for the adoption of a formula used to allocate certain expenses among the three jurisdictions served by WGL, and remand for the necessary explanation.

The ratemaking proceedings commenced on June 29, 1979, upon application by WGL for a permanent increase in its rates and charges for retail gas service within the District of Columbia. Evidentiary hearings began in January, 1980, and concluded in April, 1980. On October

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* *Associate Judge* HARRIS retired from this court effective February 5, 1982, and did not participate in the disposition of this appeal.

3, 1980, the Commission issued a Proposed Order, which was followed by a Final Order on November 10, 1980, approving a new rate schedule effective as of that date. Applications for reconsideration filed by the parties were denied on December 24, 1980, and these petitions for review followed.

WGL appeals the Commission's disallowance of increased Gas Research Institute expenses approved by the Federal Energy Regulatory Commission (FERC) and the disallowance of market pressure and flotation cost adjustments. OPC appeals the Commission's decisions concerning WGL's cash working capital allowance and the amount of the market re-entry adjustment to WGL's revenue requirement. Both parties appeal the Commission's adoption of the modified "Massachusetts Formula" to allocate a share of administrative and general expenses to District of Columbia operations.[1]

I. Scope of Review

The limited nature of our review of orders of the PSC is defined by D.C. Code 1981, § 43-906 which provides:

> [R]eview by the Court shall be limited to questions of law, including constitutional questions; and the findings of fact by the Commission shall be conclusive unless it shall appear that such findings of the Commission are unreasonable, arbitrary, or capricious.

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[1] In addition, both parties reassert their claims of error made in an appeal from a previous rate order. Our decision in *Washington Gas Light Company v. Public Service Commission*, D.C.App., ——A.2d —— (No. 79-587, Sept. 10, 1982), which issued during the pendency of this appeal is dispositive as to those "carry over issues," and we therefore do not address them on this appeal.

We have discussed the scope of our review in several opinions.[2] There is no need to repeat here what we have said before. However, one aspect of our review function bears emphasis. In *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944), the United States Supreme Court stated:

> It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. The fact that the method employed to reach that result may contain infirmities is not then important.

That language has often been quoted, and properly so, to underscore the narrow review powers of the courts in this area. Since our review power over the PSC is comparable to the authority vested in the federal courts to review Federal Energy Regulatory Commission orders, the language is applicable here. *Washington Public Interest Organization v. Public Service Commission*, D.C. App., 393 A.2d 71, 75 (1978), *cert. denied*, 444 U.S. 926 (1979). Yet the language is somewhat broad, especially in its emphasis on the end result. Obviously, it does not mean that the courts are not to review at all the methods by which the agency arrives at its result. The United States Supreme Court has recognized the regulatory commission's duty to indicate "fully and carefully the methods by which, and the purpose for which it has chosen to act."

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[2] *See Metropolitan Washington Board of Trade v. Public Service Commission*, D.C.App., 432 A.2d 343, 350-52 (1981); Also illustrative are *Washington Gas Light Company v. Public Service Commission, supra*, slip op. at 5; *People's Counsel v. Public Service Commission*, D.C.App., 399 A.2d 43 (1979); *Washington Public Interest Organization v. Public Service Commission*, D.C.App., 393 A.2d 71, 75 (1978), *cert. denied*, 444 U.S. 926 (1979).

Permian Basin Area Rate Cases, 390 U.S. 747, 792 (1968). Some elaboration is required, therefore, in order to apply the language in *Hope* to a case like the one before us.

That elaboration has been forthcoming in cases such as *Washington Public Interest Organization*, and *Mississippi River Fuel Corp. v. Federal Power Commission*, 82 U.S. App.D.C. 208, 163 F.2d 433 (1947). In the former, Judge Ferren wrote for this court:

> While it is true that a regulatory commission cannot be faulted for its methodology if the "total effect of the rate order cannot be said to be unjust and unreasonable," *Federal Power Comm'n v. Hope Natural Gas Co., supra*, 320 U.S. at 602, 64 S.Ct. at 288, it is also true that the methodology must be disclosed for the bearing it may have on that overall judgment. Absent precise explanation of methodology as applied to the facts of the case, there is no way for a court to tell whether the Commission, however expert, has been arbitrary or unreasonable. [*Washington Public Interest Organization v. Public Service Commission, supra* at 76-77.]

Earlier in *Mississippi River Fuel Corp., supra*, Judge Prettyman had written:

> . . . The discretion which must be exercised is that of the Commission. Congress has confided that function to it. At the same time, Congress has forbidden arbitrary actions and has imposed upon the courts a duty of review in that respect. Arbitrary action, if it means anything, means action not based on facts or reason. The discretion and judgment confided in the Commission must be exercised upon facts and for reason.

> The duty to review imposed upon the courts requires that the facts be found and the reasons stated. Otherwise, the courts cannot determine whether a given action is or is not arbitrary.
>
> The Congressional provisions extend to complicated, difficult matters as well as to simple questions. The courts cannot evade their responsibility merely because the subject matter is obscure. And neither can they be required to probe the minds of the agency for unfound facts or unexpressed reasons. The coordination of the two functions of administrative discretion and judicial review requires that the facts upon which the discretion is exercised, and the reasons, be clearly and completely stated. When the matter is complicated, the necessity is greater. [*Id.* at 214, 163 F.2d at 439 (footnotes omitted).]

Where the PSC has accompanied its ruling with the required full and careful explanation, that ruling is entitled to great deference. In *Metropolitan Washington Board of Trade v. Public Service Commission*, D.C.App., 432 A.2d 343, 352 (1981), Judge Gallagher stated for this court:

> Once the Commission has satisfied this initial burden and has issued a decision, however, the burden of petitioner on appeal to demonstrate reversible error is considerable. More than a difference of opinion with the Commission must be asserted, for "[t]he court's responsibility is not to supplant the Commission's balance of [the relevant public] interests with one more nearly to its liking, but instead to assure itself that the Commission has given reasoned con-

> sideration to each of the pertinent factors." *Id.* Petitioner therefore must establish "clearly and convincingly a fatal flaw in the action taken . . . ." [*Quoting Goodman v. Public Service Commission*, D.C.App., 309 A.2d 97 at 101 (1973).]

In reviewing the actions of the PSC which are the subjects of the challenges before us, we bear in mind both the deference to be paid the agency's authority and expert judgment and our responsibility to see to it that we have before us the full and careful explanation of the basis for agency action necessary to permit us to carry out the review function demanded by statute and precedent.

We will first address contentions which relate to rate base, and then proceed to issues relating to rate of return, revenues, and expenses.

II. Cash Working Capital Allowance

OPC asserts that the Commission erred in that the cash working capital allowance it awarded WGL was excessive. Cash working capital allowance is defined as "an amount which the company (investors) must supply from its *own funds* for the purpose of enabling it to meet current obligations as they arise due to the time lag between payment of expenses and collection of revenues." *People's Counsel v. Public Service Commission*, D.C.App., 399 A.2d 43, 46 (1979) (citation omitted) (emphasis in original). Since investors are entitled to a return on these advances, a cash working capital allowance is included in the rate base.

WGL requested a cash working capital allowance of $6,084,750. OPC recommended an allowance of negative $537,000. The Commission denied WGL's request for

inclusion of compensating bank balances in the allowance, but otherwise approved WGL's request and awarded the company a cash working capital allowance of $5,453,000. Although the company requested a higher amount, it does not appeal this portion of the Commission's order. OPC appeals the amount of the cash working capital allowance on five grounds.

As we noted earlier, the scope of our review is narrow. *Id.* at 45. Initially, the utility has the burden of proving its need for cash working capital. *Id.* at 47. Once the utility has borne this burden, however, and the Commission has determined the amount needed, we may not set aside the amount authorized by the Commission absent an abuse of discretion. *Id.* With these precepts in mind, we proceed to an analysis of the particular objections by the OPC to the amount of cash working capital allowance authorized by the Commission.

A. *Incremental Income Taxes*

OPC contends that the cash working capital allowance should have been reduced by the amount of the incremental income taxes associated with the increased revenues from the rate increase. The Commission, however, rejected such an adjustment, noting that additional taxes would have "no effect on the computed expense lag." The Company used a lead-lag study,[3] based upon test period experience data, to calculate the cash working capital allowance. In the lead-lag study relied upon by the Com-

[3] In a lead-lag study, the average dollar day lag in the receipt of revenues and the average dollar day lead in the payment of expenses are computed. From this, a composite expense lag is calculated. This composite expense lag is multiplied by the average daily cash requirement to determine the cash working capital allowance.

pany, dollar day lead or lag times were assigned to income tax payments and, thus, the incremental tax payments were taken into account in the Company's calculations. In choosing to credit the Company's cash working capital allowance calculation, the Commission implicitly took into consideration the fact that actual expenses and actual revenues in the utility's actual year may vary from those in the test year used in the study; this, however, should have no effect on the calculated expense lag. We defer to the Commission's use of a lead-lag methodology in calculating cash working capital alowance and, consequently, conclude that the Commission did not err in refusing to reduce the cash working capital allowance by the amount of the incremental income taxes.

B. *Gross Receipts Tax*

D.C. Code 1981, § 47-2501 provides that each gas company must make an affidavit

> on or before the 1st day of August each year as to the amount of its . . . gross earnings or gross receipts, as the case may be, for the preceding year ending the 30th day of June, and each gas company . . . shall pay to the Collector of Taxes of the District of Columbia per annum 6 per centum on such gross receipts. . . .

OPC asserts that the gross receipts taxes are paid after the money for these taxes is collected from the customers and, consequently, the cash working capital allowance should be reduced a corresponding amount. The Commission found no merit in this argument. It concluded that although the tax liability was calculated on the previous year's gross receipts, the taxes were actually paid in three advance installments. After examining the

record, we conclude that there is sufficient evidence to support the Commission's determination that the gross receipts taxes were prepaid and, consequently, should not be deducted from the cash working capital allowance.

C. *Levelized Billing Plan*

OPC also argues that WGL's use of a levelized billing plan reduces its need for cash working capital. The Commission, noting that WGL's estimate of the net expense lag was actually too low, found that OPC's proposed adjustment was not convincing in light of the other evidence introduced. Again, we find sufficient evidence in the record to support this conclusion.

D. *Jurisdictional Computation*

The Commission agreed with OPC's position that the cash working capital allowance should be calculated on a jurisdictional rather than a systemwide basis. However, in order to give WGL sufficient notice of the change, the Commission deferred implementation of the change until the next rate proceeding. OPC contends that the Commission abused its discretion in postponing the implementation of the jurisdictional computation. Finding no such abuse, we defer to the Commission's determination.

E. *Accrued Interest*

Finally, OPC asserts that the cash working capital allowance should be reduced by the amount of accrued interest owed to bondholders. In *People's Counsel v. Public Service Commission*, *supra* at 49-50, we directed the Commission's attention to *Re Iowa Power and Light Co.*, 6 P.U.R.4th 446 (1974) (deducting the amount of accrued interest on long-term debt from the cash working

capital allowance), for the Commission's "serious consideration in formulating the rate base in future proceedings." *People's Counsel v. Public Service Commission, supra* at 50. However, we declined to remand for further consideration the Public Service Commission's decision not to reduce WGL's cash working capital allowance by the amount of the accrued interest because "the matter [was] of insufficient magnitude to merit the unraveling of a complex rate structure solely on this account." *Id.*

In the proceedings being reviewed, the Commission has again declined to reduce the cash working capital allowance by the amount of the accrued interest on bonds, stating that it was "no more disposed to adopt such an argument than in the past" and citing only *People's Counsel v. Public Service Commission, supra,* and its order No. 7135 in *Re Potomac Electric Power Co.*, 36 P.U.R.4th 139 (1980). We note that in an order not cited, *Re Potomac Electric Power Co.*, 29 P.U.R.4th 517, 555-57 (1979), the Commission gave several reasons for its decision to include only cash operating expenses in the calculation of the cash working capital allowance. Essentially, the Commission concluded that interest expense is not an operating or "above the line" expense and it should not be selectively included in the cash working capital allowance, just as other "below the line" or non-cash expenses are not so included. Since the Commission has clearly articulated a basis for its treatment of accrued interest, we refer to its ruling.

In light of our analyses of the five objections OPC interposed to the Commission's determination of cash working capital allowance, we decline to overturn the Commission's ruling in that regard.

[2395]

III. Market Pressure and Flotation Costs Adjustment

WGL asserts that the Commission erred in disallowing its request for an adjustment to its rate of return for market pressure and flotation costs associated with the issuance of new stock. Market pressure refers to the depression in the price of stock which occurs when additional stock is issued; flotation costs are costs incurred in issuing the additional stock, for example, underwriting costs, attorneys' and accountants' fees, etc. When new stock is issued by a utility, these costs properly are considered in calculating the rate of return.

Among the factors a regulatory agency must consider in setting a utility's rate of return is the return an investor must receive in order to enable the utility to compete successfully for capital. The regulatory agency is obliged to allow a rate of return to equity holders that is "sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and attract capital." *Federal Power Commission v. Hope Natural Gas Co., supra* at 603. *See also Bluefield Water Works & Improvement Co. v. Public Service Commission of the State of West Virginia*, 262 U.S. 679 (1923).

The rate of return required to attract capital investment is referred to as the "cost of equity." The Commission calculated WGL's cost of equity by the discounted cash flow (DCF) method. That method takes into account an investor's anticipated income from dividends and capital gain upon eventual sale of the stock in order to arrive at an estimated rate of return which the investor must receive in order to induce him to invest in the utility stock. The cost of equity arrived at by the DCF method is referred to as the "bare-bones" cost of equity, *i.e.*, the cost of equity determined solely on the basis of current

dividend returns and anticipated growth, without adjustment for factors such as the issuance of additional stock.

In the instant case, the Commission set the cost of equity to WGL as a return on equity of 13.25%.[4] WGL does not appeal this determination of the "bare-bones" cost of equity, but appeals the Commission's refusal to adjust the rate of return upward to reflect market pressure and flotation costs expected to result from WGL's anticipated issuance of additional common stock in 1981. The Commission concedes that the rate of return allowed to equity holders should include an allowance for market pressure and flotation costs when additional stock is issued, but justifies its refusal to grant the allowance here on the grounds that WGL did not present sufficient evidence that it would issue additional stock in the near future to warrant granting the allowance.[5]

The record reflects that WGL Chief Financial Officer, Patrick J. Maher, in testimony filed with the Commission on March 31, 1980, stated that WGL planned a public offering of common stock in 1981, and that on April 8, 1980, Mr. Maher testified that a five-year plan to issue stock, including a projected issuance of fifteen to twenty million dollars worth of common stock in 1981, had been approved by the WGL Board of Directors in March, 1980.

In its Proposed Order, the Commission noted that Mr. Maher was "probably in the best position to determine

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[4] Commission's Final Order No. 7209, ordering paragraph B, at 2, Nov. 10, 1980.

[5] Commission's Proposed Order No. 7193, ordering paragraph D, at 32, Oct. 3, 1980.

[WGL's] need for new equity," and that he "indicated quite strongly" that approximately fifteen to twenty million dollars in new equity would be needed in 1981. Yet, the Commission concluded that the evidence submitted to it indicated "little more than a possibility" of a new issuance of common stock.[6] We disagree. The evidence before the Commission in the form of testimony of the company's Chief Financial Officer was that the Board of Directors had approved the issuance of common stock having a value of approximately fifteen to twenty million dollars. As the Commission itself concedes, WGL's failure to announce a more specific plan regarding the issuance was "not unusual since such information commonly is released only shortly in advance [of actual issuance]."[7]

We conclude that the evidence concerning WGL's projected issuance of common stock in 1981 was such that it was unreasonable for the Commission to deny an adjustment to the rate of return to reflect the market pressure and flotation costs associated with the issuance.[8] We hold, therefore, that the Commission's refusal to grant the adjustment was error.

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[6] *Id.*

[7] *Id.*

[8] In our review of the evidence before the Board on this issue, we did not consider Mr. Maher's reported statement to the Maryland Public Service Commission, as represented to the Commission by WGL in its Exceptions to the Commission's Proposed Order, nor did we consider WGL's application to the Commission in March, 1981, for authorization to issue new common stock; the statement and application were not properly before the Board as evidence in the proceedings under review here.

IV. Market Re-Entry

OPC contends that the Commission's decision to reduce WGL's revenue requirement by only $600,000 by reason of market re-entry was not supported by substantial evidence. The term market re-entry as used here refers to the anticipated growth in sales expected to be realized by WGL as a result of relaxation of restrictions on the Company's extension of its service to new customers. The restrictions were imposed by the Commission in 1972 due to a shortage of natural gas. As the availability of gas increased, the restrictions were eased and, in 1978, the Commission approved a plan for gradual increase in the number of WGL customers.

Additional sales by WGL under the program began in approximately October, 1979, and were considered in the calculation of the Company's cost-of-service for 1979. In addition, the Commission reduced the Company's annual revenue requirement by $600,000 in consideration of prospective sales increases. WGL does not appeal the Commission's order with respect to the adjustment to the revenue requirement. OPC, however, contends that the Commission's decision is unsupported by substantial record evidence.

In proceedings before the Commission, WGL contended that no revenue adjustment was necessary to account for market re-entry. At the same time the Company projected an increase in future sales which the Commission calculated would have the net effect of reducing the revenue requirement by $423,891 annually. Commission staff estimated a gross increase in Company revenues of $5,896,000 annually resulting in a net reduction to the revenue requirement of approximately $795,000 annually. OPC projected a $6,444,000 annual increase in gross revenues with a resultant reduction to revenue requirement of $927,872.

The requirement of the District of Columbia Administrative Procedure Act, D.C. Code 1981, § 1-1509(e), that agency decisions be accompanied by findings of fact and supported by substantial evidence imposes upon the agency the duty to make findings of basic facts upon which the agency decision rests. Put another way, the agency must "show on what it relied in reaching its decision." *Citizens Association of Georgetown, Inc. v. District of Columbia Zoning Commission*, D.C.App., 402 A.2d 36, 42 (1979), *quoting Miller v. Commission on Human Rights*, D.C. App., 339 A.2d 715, 719 (1975). Moreover, the agency decision must rationally follow from the facts. *Citizens Association of Georgetown, Inc. v. District of Columbia Zoning Commission, supra* at 41.

In its Proposed Order, the Commission set forth findings of fact and cited to record evidence in support of its determination that the estimates of future sales provided by the parties were deficient.[9] The Commission's stated reasons for ordering a $600,000 reduction to WGL's revenue requirement were that the net effect of the sales growth forecast by WGL was "too conservative;" the estimates by staff and OPC might prove to be "unrealistically high:" an increase in sales was "a virtual certainty," and the rate of growth in sales was "slower than anticipated." The Commission made no express findings, however, to underpin the revenue adjustment it ultimately ordered.

Thus, there is some merit in OPC's contention that the Commission's conclusion is not properly supported by its findings. We must recognize, at the same time, that implicit in its determination of a revenue requirement reduction is a PSC estimate of the amount of sales growth WGL will experience due to its re-entry into the market.

[9] Order No. 7193 at 35-40.

The record provided the Commission with sufficient evidence on the market re-entry issue to provide an adequate basis for decision, although, necessarily, the evidence consisted in large part of estimates and projections. In view of the Commission's implicit finding as to sales growth, we decline to set aside its decision in this regard.

V. Gas Research Institute Expenses

WGL challenges the Commission's refusal to allow the company to recover, as operating costs, projected increases in the wholesale cost of natural gas attributable to increases in Gas Research Institute surcharges effective January 1, 1981. The Commission limited the Company's recovery to the "current amount" of Gas Research Institute surcharges, *i.e.*, the amount paid by WGL in the test year, 1979, approximately $93,000.[10]

The Gas Research Institute (GRI) is a non-profit research and development corporation supported by the natural gas industry. Its members include interstate pipeline and distribution companies. GRI's costs are assessed its members who, in turn, incorporate the cost of their contributions into the rates they charge their retail utility customers such as WGL. Before the interstate wholesalers can raise their rates to reflect increases in their assessed contributions, they must receive approval from FERC.[11]

The Natural Gas Act, 15 U.S.C. §§ 717 *et seq.* (1976), authorizes FERC to regulate the interstate transporta-

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[10] Commission Order 7209, ordering paragraph E at 4 (November 10, 1980).

[11] The FERC was created pursuant to 42 U.S.C. §§ 7101 *et seq.* (Supp. II 1978) and Executive Order No. 12009, 42 Fed. Reg. 46267 (1977), and as of October 1, 1977, assumed the functions of the Federal Power Commission (FPC).

tion and sale of natural gas, including approving rates charged in interstate sales. So that wholesale companies need not petition FERC for permission to raise their rates whenever their assessed contributions are raised, FERC allows research and development corporations such as GRI to submit to FERC for approval a proposed budget, including contributions assessments. FERC approval of the research and development organization's plan constitutes approval of the member companies' contributions to the organization, including the wholesale rate increase reflecting the higher assessments.

Since a wholesaler's rates reflect contributions to GRI, any increase in GRI costs to the wholesaler results in a higher purchase cost of gas to the local utility. The local utility's purchase cost is an operating expense and is properly included in the cost of service.

WGL purchases natural gas from two wholesale companies, Columbia Gas Transmission Corporation and Transcontinental Gas Pipeline Corporation. Both wholesalers are members of GRI. In September 1980, FERC approved an increase in GRI assessments from .048 per Mcf.[12] to .056 cents per Mcf. effective January 1, 1981.[13] In the ratemaking proceeding under review here, WGL requested that it be allowed to raise its rates to reflect the correspondingly increased wholesale costs resulting from the increased GRI surcharges approved by FERC.[14] The Commission granted WGL permission to charge rates reflecting the Company's GRI contribution as of October,

[12] One Mcf. is 1,000 cubic feet.

[13] FERC Opinion No. 96, Ordering Paragraph (B) at 18 (Sept. 30, 1980).

[14] WGL estimated its yearly contributions to GRI from 1980 to 1984 inclusive, to be: 1980—$127,109; 1981—$175,665; 1982—$213,930; 1983—$246,846; 1984—$254,162.

1979, but refused to allow an adjustment to reflect the increase effective January, 1981. The Commission justified its decision on the grounds that the FERC approved increase was not a "known and measurable expense," and that few benefits would accrue to District of Columbia ratepayers as a result of GRI activities.

The Commission agrees that the entire wholesale cost of gas is recoverable by WGL as a cost of service. It is the Commission's position, however, that the authority of FERC to approve GRI charges to member companies was in question at the time of the present ratemaking proceeding, and thus that portion of wholesale costs attributable to GRI charges was not a measurable and certain expense. The Commission further contends that, even if FERC is found to have authority to approve the GRI increase, the Commission acted properly in denying the GRI charges and that the correct procedure was for the Company to return to the Commission and ask for a rate increase when the issue of FERC jurisdiction was settled.

At the time the Commission issued its order, a suit was pending in the United States Court of Appeals for the District of Columbia Circuit challenging FERC's jurisdiction to approve GRI charges to member companies. Subsequent to the Commission's order in the present case, the court ruled that FERC has jurisdiction to approve GRI's program and budget and to rule on applications for rate increases submitted by GRI on behalf of the jurisdictional members. *Public Utilities Commission of the State of Colorado v. Federal Energy Regulatory Commission*, 660 F.2d 821, 825 (D.C.Cir. 1981), *cert. denied*, —— U.S. ——, 102 S.Ct. 2009 (1982).[18]

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[18] We agree with OPC that nothing in the holding of the case can be read as extending FERC's jurisdiction to the issue

The issue before us is whether the Commission erred in disallowing the increased GRI charges as reasonable operating expenses on the grounds that the above appeal was pending at the time of the Commission's decision. We hold that it did. It is well settled that the Natural Gas Act provides for exclusive federal regulation of interstate wholesales of natural gas. *See Northern Natural Gas Company v. State Corporation Commission of Kansas*, 372 U.S. 84 (1963); *Illinois Natural Gas Company v. Central Illinois Public Service Commission*, 314 U.S. 498 (1942). State and local commissions have no authority, therefore, to inquire into the reasonableness of wholesale rates, but must allow them as reasonable operating expenses. *See, e.g., Citizens Gas Users Association v. Public Utilities Commission of Ohio*, 165 Ohio St. 536, 138 N.E. 2d 383 (1956); *City of Chicago v. Illinois Commerce Commission*, 13 Ill.2d 607, 150 N.E.2d 776 (1958); *United Gas Corp. v. Mississippi Public Service Commission*, 127 So.2d 404 (Miss. 1961).[16]

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of whether increased wholesale costs shall be passed through to retail customers by the local utility. The determination of the extent to which wholesale costs should be reflected in local utility rates lies exclusively with local utility commissions. *See Narragansett Electric Co. v. Burke*, 381 A.2d 1358, 1363 (R.I. 1977), *cert. denied*, 435 U.S. 972 (1978).

The Commission's refusal to allow increased GRI charges to be reflected in retail rates in the instant case, however, was based upon the Commission's erroneous conclusion that the increase in wholesale costs was not a just and reasonable operating expense, rather than upon a determination that the expense should not be passed through to retail customers.

[16] The highest courts of at least two jurisdictions have held that state utility commissions are not free to disallow, as operating expenses, wholesale rates filed with, but not yet approved by, the FERC. *See Narragansett Electric Co. v. Burke, supra; United Gas Corp. v. Mississippi Public Service Comm'n., supra.*

In the instant case, the Commission chose to disregard a final FERC order approving wholesale rates on the ground that FERC's jurisdiction had been challenged by another utility commission in a petition for judicial review of the order. The Commission ignored the fact that in the absence of a stay the FERC order, as a final agency order, was fully in effect during proceedings for review. *Jupiter Corp. v. Federal Power Commission*, 137 U.S.App.D.C. 295, 303, 424 F.2d 783, 791 (1969), *cert. denied*, 397 U.S. 937 (1970); *Ecee, Inc. v. Federal Power Commission*, 526 F.2d 1270, 1274 (5th Cir.), *cert. denied*, 429 U.S. 867 (1976).

We hold that the Commission had no authority to disallow as a reasonable operating expense the wholesale purchase cost of natural gas approved by FERC, including that portion of wholesale costs attributable to GRI surcharges to become effective January 1, 1981. Because we hold that the Commission had no jurisdiction to rule on the reasonableness of such surcharges, we need not reach, and the Commission was unauthorized to consider, the issue whether the GRI charges benefit the District of Columbia ratepayers.

Finally, we decline PSC's invitation to rule that the United States Court of Appeals erred in *Colorado* and to hold that FERC was without jurisdiction to approve GRI expenses as a part of the wholesale rate paid by gas retail companies including WGL. Review of the rulings of FERC is vested by statute in the United States Court of Appeals, not this court. *See* 15 U.S.C. § 717r(b) (1976).

VI. Modified Massachusetts Formula

WGL serves consumers in the District of Columbia, Maryland and Virginia. Both WGL and OPC assert that the Commission erred in adopting a new formula for al-

locating to the District of Columbia its fair share of administrative and general [A&G] expenses.

In Formal Case No. 686, the Commission directed WGL to:

> [E]ither reflect A&G expenses allocation solely according to a modified "Massachusetts Formula" or if it nonetheless still advocate[d] a different approach, present a complete alternate cost of service which reflects allocation under modified "Massachusetts Formula." [Commission Order No. 6051, ordering paragraph C at 76.]

The Massachusetts Formula, originally used by the Massachusetts Department of Revenue to determine the amount of tax owed to Massachusetts by corporations doing some of their business in the state, allocates administrative and general expenses by employing an average of the percentage of property, wages and (twice the percentage of) sales related to the jurisdiction. Formerly, the Commission had permitted WGL to allocate administrative expenses not directly assignable to a jurisdiction on the basis of a factor, expressed in terms of labor expenses, which was a composite of a number of factors including therm sales, plant, and labor. At the rate proceeding below, WGL continued to use its existing method for allocating A&G expenses and presented a comparative statement showing the revenue requirement using the "Massachusetts Formula" for allocating A&G expenses. OPC advocated that all A&G expenses—both labor-related and non-labor-related—be allocated according to the modified Massachusetts Formula and that an adjustment of $1.5 million be made to the revenue requirement.

In its order the Commission purported to adopt a modified Massachusetts Formula, and stated that it allocated labor-related A&G expenses in the same manner as all A&G expenses had been allocated in the past and non-labor-related expenses on the basis of a simple average of the jurisdiction's share of plant, sales and labor.[17] The Commission reduced WGL's allocation of A&G expenses to the District of Columbia by $856,000. WGL contends that the Commission's decision to adopt the modified Massachusetts Formula for allocating A&G expenses is not supported by substantial evidence, lacks the requisite findings of fact and jeopardizes the company's ability to recover its cost of service in the Washington metropolitan area. OPC supports the use of the modified Massachusetts Formula, but argues that the record does not support the amount of the adjustment made by the Commission.

As we observed in the discussion above of the scope of our review, "[b]efore meaningful judicial review to determine the reasonableness of a Commission decision is possible, the Commission, of course, must satisfy its own burden: to base its decision on sufficient evidence and to explain its actions 'fully and carefully.'" *Metropolitan Washington Board of Trade v. Public Service Commission, supra* at 351; *See Washington Public Interest Organization v. Public Service Commission, supra* at 75-78; *Mississippi River Fuel Corp. v. Federal Power Commission,*

[17] OPC questions the Commission's actual application of the Modified Massachusetts Formula. Although the Commission gave a general description of its concept of the Modified Massachusetts Formula in its order, it failed to elaborate on its methodology, *i.e.*, disclosure of the percentages of revenue, plant and labor allocated to each jurisdiction, and a breakdown of the administrative and general expenses subaccounts into labor and non-labor-related expenses.

supra at 224, 163 F.2d at 433. Although our review function is narrow, before we can give deference to the Commission's choice of methodology, that methodology must be fully disclosed. *Washington Public Interest Organization v. Public Service Commission, supra* at 76-77.

In its order, the Commission failed to explain the reasons for its choice of the so-called Modified Massachusetts Formula, the method it used to employ that formula, and the calculation of the amount of the adjustment to the District's share of A&G expenses.[18] In the absence of such an explanation, it is impossible for us to determine whether the Commission's choice of the Modified Massachusetts Formula is reasonable. Therefore, we must remand the case to the Commission for an explanation of precisely what formula was used, why that formula was chosen, and how the amount of the adjustment was computed. *See Washington Public Interest Organization v. Public Service Commission, supra* at 78; *Mississippi River Fuel Corp. v. Federal Power Commission, supra* at 227, 163 F.2d at 436.

VII. Remedy

We reverse the Commission's refusal to adjust the rate of return to reflect market pressure and flotation costs associated with the issuance of common stock and its disallowance of the projected increases in GRI surcharges as operating expenses. In light of the relatively small amounts of revenue involved, *see People's Counsel v. Public Service Commission, supra* at 50, and the policy against retroactive ratemaking, *see Bebchick v. Washing-*

[18] From its order, it is impossible for us to determine which party's exhibits and calculations, if any, the Commission credited and relied upon in adopting its version of the Modified Massachusetts Formula.

ton Metropolitan Area Transit Commission, 158 U.S.App. D.C. 79, 85, 485 F.2d 858, 864 (1973); *Payne v. Washington Metropolitan Area Transit Commission*, 134 U.S. App.D.C. 321, 329-31, 415 F.2d 901, 909-11 (1968), however, we do not remand these aspects of the order for recalculation of the revenue requirement.[10]

We remand the Commission's adoption of the Modified Massachusetts Formula for an explanation of its reasons for choosing this formula. In this regard, we note that we have

> not reversed the conclusions of the Commission, except in the procedural sense necessary to a remand. [We have] remanded the case for clarification where clarity is not present, and for completion where incompleteness now exists. When the findings and conclusions are complete and clear, the court will then, if appropriate proceedings are brought, consider whether the ultimate rulings of the Commission are within the permissible bounds of its power. [*Mississippi River Fuel Corp. v. Federal Power Commission, supra* at 227, 163 F.2d at 452.]

See also Washington Public Interest Organization v. Public Service Commission, supra.

In all other respects, the order under review is affirmed.

Affirmed in part; reversed in part; remanded for further proceedings in part.

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[10] We observe that, in view of our rulings herein, there is no aspect of the GRI or market pressure-flotation cost issues that will require PSC consideration upon our remand on the issue of allocation of A&G expenses.

DISTRICT OF COLUMBIA COURT OF APPEALS
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DISTRICT OF COLUMBIA
COURT OF APPEALS
FILED JAN 21 1983
Clerk

Nos. 81-229 and 81-232

WASHINGTON GAS LIGHT COMPANY, Petitioner,

v.

PUBLIC SERVICE COMMISSION OF THE DISTRICT OF COLUMBIA, Respondent.

OFFICE OF PEOPLE'S COUNSEL, Intervenor.

BEFORE: Newman, Chief Judge; *Kelly, Kern, Nebeker, Mack, Ferren, Pryor, *Belson, and Terry, Associate Judges.

ORDER

On consideration of respondent's petition for rehearing or rehearing en banc and the supplemental memorandum in support thereof, it is

ORDERED for the merits division* that respondent's petition for rehearing is denied; it appearing that no judge of this court has called for a vote thereon, it is

FURTHER ORDERED that respondent's petition for rehearing en banc is denied.

PER CURIAM

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APPENDIX

Excerpt from Proposed Final Order in F.C. No. 722

Order No. 7193

F. *Gas Research Institute*

The Gas Research Institute (GRI) was formed in 1977 to coordinate and accelerate critically needed research into gaseous fuels. It replaced the American Gas Association's efforts in this area. The membership of GRI consists of 137 distribution companies, 28 interstate pipeline companies and 24 municipal utilities and represents the vast majority of gaseous fuel suppliers in the United States. WGL is a member as is Columbia and Transco, WGL's pipeline suppliers. The research and development program under GRI is reviewed by its advisory council, research coordination panel, industry technical advisory committee, and municipal gas system advisory committee, which evaluate GRI research from the viewpoints of economic, consumer, environmental, scientific, industrial and regulatory interests.

WGL states that each year GRI submits its five-year research plan and budget to FERC for review and approval to insure that the its activities are prudent, well-designed, and in the public interest. Once approved, the costs of funding the research program are embodied in the wholesale cost of gas. WGL is thereafter assessed by its pipeline suppliers for these charges as part of its gas bills. WGL's portion of the charges as part of its gas bills. WGL's portion of the costs through October 1979 which is allocated to the District of Columbia operations is $93,000 (WGL Exh. H, p. 7). However, GRI's budget continues to

grow throughout its most recent five-year forecast period and, with it, WGL's share. Thus, WGL's projected contributions to G.R.I. on a D.C. basis are $127,109 for 1980, $175,665 for 1981, $213,930 for 1982, $246,846 for 1983, and $254,162 for 1984 (OPC brief, p. 233.)

WGL argues that a utility is entitled to charge all of its legitimate operating expenses to its ratepayers and that its GRI assessment is no different than the expenses it incurs for any other utility operation. It cites *Mississippi Fuel Corporation v. FPC,* 163 F.2d 433 at 437 (D.C. Cir. Ct. 1947) and *West Ohio Gas Company v. Ohio Public Utilities Commission,* 294 U.S. 63 at 72 (1975) for the proposition that the allowed return on investment, which is that amount over and above expenses, must be proved and that the court — and presumably this regulatory agency — should not substitute is judgment for a utility's as to the appropriate amount of an expenditure.

WGL claims that were it not to pay its assessment it would not be able to buy its gas supplies, in that the assessment is merely one component of WGL's commodity cost of gas which it is legally entitled to recover. WGL claims that neither the District of Columbia Commission nor the company has any control or any right of control over the company's commodity costs except to the extent that each, by intervention in federal rate proceedings, exercises its powers of persuasion.

WGL maintains that the GRI research and development programs benefit the ratepayers by improving the gas supply, promoting the conservation of natural gas and safety programs, improving environmental quality, and eliminating fragmented and often duplicative research which individual companies might otherwise undertake. In view of the foregoing, WGL maintains that the entire

amount allocated to GRI in its cost of service study should be allowed by the Commission.

Staff's position is similar to that of WGL. Staff argues that the Federal Energy Regulatory Commission has specifically authorized the GRI surcharge for interstate gas as a reasonably incurred operating expense under the "filed rate doctrine." The charge, staff maintains, is also recognized as a component of the legal rate charged to WGL. *Narrangansett Electric Company v. Bruke,* 381 A.2d 1358, 1362 (R.I. 1977), *cert. denied* 435 U.S. 972 (1978). Staff also agrees with WGL that as the company has no realistic choice but to pay the rate included in the GRI charge, equity would demand that these increased costs be recovered in a rate adjustment.

OPC equates this issue with the AGA expense issue, in that WGL has to carry the burden on the record of the propriety of these expenses. OPC cites the case of *Re: Western Slope Gas Company* (Decision No. C79-907, 1979), a Colorado decision which denied a utility its request for automatic flow-through of the GRI assessment but did permit the company to set out the charge in the context of the general revenue investigation. OPC maintains that the record in this proceeding has failed to specify or quantity potential benefits to customers from WGL's participation in GRI. OPC submits that D.C. ratepayers can expect little or no benefits from WGL's proposed funding of GRI.

OPC maintains that the benefits of GRI will go to manufactures first, appliance dealers second and WGL and its ratepayers third. The benefit wold flow through to the ratepayer only to the extent that he utilizes and purchases the new, efficient gas appliances.

OPC contends that the Commission's duty to establish rates has not been usurped by the actions of FERC in approving the GRI budget. OPC submits that the District of Columbia Commission has independent authority to determine the ratemaking treatment of GRI on its own, irrespective of the manner in which FERC has decided the issue. OPC concedes, however, that there is controversy over the question of whether the FERC decision preempts this Commission from disallowing the GRI contribution. This preemption is being challenged in the case of *State of Colorado v. FERC (D.C. Cir., C.A. No. 80-117). OPC* would have the Commission reserve decision on this matter and render a separate decision when the legal authority issue is resolved by the court in the above captioned case.

We do not contest the viability of the proportionate assessment by WGL's pipeline suppliers of its share of GRI's annual costs. We also are aware that FERC has decided not to mandate shareholder contributions by its member companies to meet GRI's annual budgetary needs.[37] Such action, however, does not predetermine our obligation to assure that the D.C. ratepayers are charged no more than is reasonably necessary by WGL for the maintenance of safe, efficient and adequate gas service. We recognize that the GRI program may provide some benefits to ratepayers in the future. Nevertheless, insofar as the immediate consumer is concerned, these benefits are indirect at best and, in our opinion, will be substantially less to residential consumers — which comprise the majority of WGL's customers, both in terms of absolute

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[37]Gas Research Institute, *Order Denying Request to Require Shareholder Contributions*, Docket No. RP 78-76, issued May 23, 1979.

numbers and in volumes of gas consumed – than they will be to industrial and commercial customers and to the gas utility companies in general.

In Order No. 6051, pp. 69-71, we considered whether certain payments made by WGL to the American Gas Association in support of its activities were properly included as an expense to be charged to WGL's ratepayers. We concluded that they should not be so charged because there was no evidence that the activities financed served to improve customer service. Although GRI's program differs in major respects from that of AGA, the principle underlying the decision on cost recovery is the same.

In our opinion WGL and its stockholders stand to receive a substantially greater benefit from the company's participation in GRI than will the customers themselves. Nevertheless, at this time WGL's share of GRI's costs is relatively small – $93,000 – and a number of activities being engaged in by GRI do hold at least a promise of providing some general benefit to all gas consumers, including those of WGL. Accordingly, we shall allow the current amount in this case as part of the wholesale commodity cost of gas to the company. Any increases above this amount will be considered in later cases. In addition, we will expect WGL to review critically GRI's annual budgetary submissions and to participate fully in any proceedings on this subject before that agency.

Excerpt from Final Order In F.C. No. 722

Order No. 7209

E. *Gas Research Institute*

In Order No. 7193 we concluded that WGL should be permitted to recover the "current amount" of the charges included in its wholesale gas cost which is utilized to meet the operational costs of the Gas Research Institute. This current rate is 0.047 cents per therm which in 1979 amounted to $93,000, allocated to WGL's operations in the District. We also stated that any increases above the current amount " . . . will be considered in later rate cases." Order No. 7193, p. 61. WGL notes that the charges it must pay have already been increased, effective January 1, 1981, and requests that it be permitted to collect the effective GRI portion of its wholesale gas rates as fixed from time to time by appropriate authority.

WGL's exception is denied. We are aware (and were aware at the time the Proposed Opinion issued) that the per therm assessment would be increased effective January 1, 1981. Nevertheless, no increase over the current per therm charge was authorized since the increase has not been proven on the information before us and, although approved by FERC, has not been shown to be justified on a record before this Commission. Absent such justification we have no way of evaluating the merit of the increase or the proper amount to be accepted as allocable to District of Columbia ratepayers.

Excerpt From Order Denying Reconsideration in F.C. No. 722

Order No. 7237

As noted earlier, WGL objects to our decision not to reflect in these rates the increased GRI funding jassessment it will beging paying on January 1, 1981, as part of its pipeline suppliers' FERC filed rates. We do not accept this adjustment as a known change, required to be reflected in these rates. Although the Supreme Court of Rhode Island in *Narragansett Electric Co. v. Burke,* 381 A.2d 1358 (RI. 1977), *cert. denied,* 435 U.S. 972 (1978), rejected an attempt by that state's commission to deny recovery in retail rates of any portion of the FERC-established wholesale rates. We believe that the issued of WGL's assessment rate for the support of GRI has not been finally resolved. The FERC approved rate is undergoing judicial review. See *Colorado PUC v. FERC,* CADC, No. 80-1117; see also *Office of Consumers' Counsel v. FERC,* ____ Fed.2d ____, CADC, No. 80-1303, et al issued December 8, 1980. Assuming the revised rate is overturned, WGL, not having paid the increase, will not be required to make refunds to its customers. If the rate is sustained, WGL can seek current recovery via the filing of a proper rate change request. The fact that an exact matching of cost and revenues may not take place provides no basis for an additional allowance under existing circumstances.

Natural Gas Act § 2, 15 U.S.C. § 717a. Definitions

When used in this chapter, unless the context otherwise requires -

(1) "Person" includes an individual or a corporation.

(2) "Corporation" includes any corporation, joint-stock company, partnership, association, business trust, organized group of persons whether incorporated or not, receiver or receivers, trustee or trustees of any of the foregoing, but shall not include municipalities as hereinafter defined.

(3) "Municipality" means a city, county, or other political subdivision or agency of a State.

(4) "State" means a State admitted to the Union, the District of Columbia, and any organized Territory of the United States.

(5) "Natural gas" means either natural gas unmixed, or any mixture of natural and artificial gas.

(6) "Natural-gas company" means a person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale.

(7) "Interstate commerce" means commerce between any point in State and any point outside thereof, or between points within the same State but through any place outside thereof, but only insofar as such commerce takes place within the United States.

(8) "States commission" means the regulatory body of the State or municipality having jurisdiction to regulate rates and charges for the sale of natural gas to consumers within the State or municipality.

(9) "Commission" and "Commissioner" means the Federal Power Commission, and member thereof, respectively.

Natural Gas Act § 4, 15 U.S.C. § 717c. Rates and charges; schedules; suspension of new rates

(a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from June 21, 1938) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, State commission or gas distributing company, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would

otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may by order require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

Natural Gas Act § 8, 15 U.S.C. § 717g. Accounts; records; memoranda

(a) Every natural-gas company shall make, keep, and preserve for such periods, such ac-

counts, records of cost-accounting procedures, correspondence, memoranda, papers, books, and other records as the Commission may by rules and regulations prescribe as necessary or appropriate for purposes of the administration of this chapter: Provided, however, That nothing in this chapter shall relieve any such natural-gas company from keeping any accounts, memoranda, or records which such natural-gas company may be required to keep by or under authority of the laws of any State. The Commission may prescribe a system of accounts to be kept by such natural-gas companies, and may classify such natural-gas companies and prescribe a system of accounts for each class. The Commission, after notice and opportunity for hearing, may determine by order the accounts in which particular outlays or receipts shall be entered, charged, or credited. The burden of proof to justify every accounting entry questioned by the Commission shall be on the person making, authorizing, or requiring such entry, and the Commission may suspend a charge or credit pending submission of satisfactory proof in support thereof.

(b) The Commission shall at all times have access to and the right to inspect and examine all accounts, records, and memoranda of natural-gas companies; and it shall be the duty of such natural-gas companies to furnish to the Commission, within such reasonable time as the Commission may order, any information with respect thereto which the Commission may by order require, including copies of maps, contracts, reports of engineers, and other data, records, and papers, and to grant to all agents of the Commission free access to its property and its ac-

counts, records, and memoranda when requested so to do. No member, officer, or employee of the Commission shall divulge any fact or information which may come to his knowledge during the course of examination of books, records, data, or accounts, except insofar as he may be directed by the Commission or by a court.

(c) The books, accounts, memoranda, and records of any person who controls directly or indirectly a natural-gas company subject to the jurisdiction of the Commission and of any other company controlled by such person, insofar as they relate to transactions with or the business of such natural-gas company, shall be subject to examination on the order of the Commission.

Natural Gas Act § 16, 15 U.S.C. § 717(c). Administrative powers of Commission; rules, regulations, and orders

The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this chapter. Among other things, such rules and regulations may define accounting, technical, and trade terms used in this chapter; and may prescribe the form or forms of all statements, declarations, applications, and reports to be filed with the Commission, the information which they shall contain, and the time within which they shall be filed. Unless a different date is specified therein, rules and regulations of the Commission shall be effective thirty days after publication in the manner which the Commission shall prescribe. Orders of the Commission shall be effective on the date and in the manner which

the Commission shall prescribe. For the purposes of its rules and regulations, the Commission may classify persons and matters within its jurisdiction and prescribe different requirements for different requirements for different classes of persons or matters. All rules and regulations of the Commission shall be filed with its secretary and shall be kept open in convenient form for public inspection and examination during reasonable business hours.